

Auditor-General of South Africa

Mpofana Municipality - Audit report 2016-17

Report of the auditor-general to the KwaZulu-Natal Provincial Legislature and the council on Mpofana Municipality

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Mpofana Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2017, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget information with actual information for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the possible effects of the matters described in the basis for qualified opinion section of this report, the financial statements present fairly, in all material respects, the financial position of the Mpofana Municipality as at 30 June 2017, and its financial performance and cash flows for the year then ended in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2016 (Act No. 3 of 2016) (DoRA).

Basis for qualified opinion

Property, plant and equipment

3. The municipality did not depreciate property, plant and equipment, as required by GRAP 17, *Property, plant and equipment*. The effect on the financial statements was that property, plant and equipment closing balance was understated by an estimated amount of R3,58 million. There was a resultant impact the accumulated surplus. Additionally, I was unable to obtain sufficient appropriate audit evidence for the capital work in progress included in the property, plant and equipment due to the status of the accounting records. I was unable to confirm the capital work in progress by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to property, plant and equipment stated at R155,39 million in the financial statements.

Receivables from exchange and non-exchange transaction

4. I was unable to obtain sufficient appropriate audit evidence as the receivables from exchange and non-exchange transactions did not reconcile to debtors age analysis. I was unable to confirm these receivables by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to receivables stated at R13,46 million and R25,37 million respectively in notes 5 and 7 to the financial statements. The resultant impact on the revenue and impairment could not be determined.

Payables from non-exchange transactions – leave pay provision

5. I was unable to obtain sufficient appropriate audit evidence that the leave pay provision included in the payables from non-exchange transactions had been properly accounted for, due to the status of the accounting records. I was unable to confirm the leave pay provision by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to leave pay provision stated at R3,46 million disclosed in note 15 to the financial statements.

Revenue - Licence and permit

6. I was unable to obtain sufficient appropriate audit evidence that licences and permits had been properly accounted for, due to the status of the accounting records. I was unable to confirm licences and permits by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to revenue stated at R3,20 million to the financial statements.

Expenditure - General expenses

7. I was unable to obtain sufficient appropriate audit evidence for general expenses, as requested information was not submitted timeously. I was unable to confirm the general expenses amount by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to general expenses stated at R29,73 million disclosed in note 36 to the financial statements.

Irregular Expenditure

8. The municipality did not include all the irregular expenditure in the notes to the financial statements, as required by section 125(2)(d) of the MFMA. This resulted from payments made in contravention of the supply chain management requirements. I was unable to confirm this amount by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the irregular expenditure stated at R32,50 million disclosed in note 45 to the financial statements.

Context for the opinion

9. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of this report.
10. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) and the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.
11. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Material uncertainty relating to going concern

12. I draw attention to note 49 in the financial statements, which indicates that the municipality's current liabilities exceeded its total assets by R45,66 million. The municipality is not able to meet its liabilities as they fall due. The lack of sufficient funds also means that the municipality is unable to meet its consumer deposits and landfill site provision obligations. As stated in note 49, these events or conditions, along with other matters as set forth in note 49, indicate that a material uncertainty exists that may cast significant doubt on the municipality's ability to continue as a going concern.

Emphasis of matter

13. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Material impairments

14. As disclosed in note 5 and 7 to the financial statements, the municipality recognised allowance for impairment of R13,46 million and R44,67 million respectively for the receivables from exchange and non-exchange transactions as the recoverability of these amounts was doubtful.

Other matters

15. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Unaudited disclosure notes

16. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion thereon.

Responsibilities of the accounting officer for the financial statements

17. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA, DoRA and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.
18. In preparing the financial statements, the accounting officer is responsible for assessing the Mpoofana Municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the intention is to liquidate the municipality or cease operations, or there is no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

19. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.
20. A further description of my responsibilities for the audit of the financial statements is included in the annexure to this auditor's report.

Report on the audit of the annual performance report

Introduction and scope

21. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected development priority presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
22. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators/measures included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.
23. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for basic services delivery presented in the annual performance report of the municipality for the year ended 30 June 2017.
24. I performed procedures to determine whether the reported performance information was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
25. The material findings in respect of the usefulness and reliability of the selected development priority are as follows:

Basic service delivery

Various indicators: Performance indicators are not well defined

26. The source information and method of calculation for the achievement of the following planned indicators was not clearly defined, as required by the Framework for managing programme performance information (FMPPI).

■ Number of new Consumer Units with access to Refuse Removal ■ Completed Phase 1 of Sthembiso-Cabazini Road (Tarring) ■ Gravelled (Nkandla) Gravel Road ■ Rehabilitated Mangaung Access Road (Phase 1) Tarring

Number of new consumer units with access to electricity

27. I was unable to obtain sufficient appropriate audit evidence for the reported achievement for the target of 242 units. This was due to incomplete listing provided to support the reported achievement and lack of appropriate supporting evidence. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievement of 242 units

Number of new consumer units with access to refuse removal

28. I was unable to obtain sufficient appropriate audit evidence for the reported achievement for the target of 71 Consumer Units. This was due to incomplete listing provided to support the achievement and lack of sufficient appropriate evidence to support action achievement. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievement of 71 consumer units.

Other matters

29. I draw attention to the matters below.

Achievement of planned targets

30. The annual performance report on pages x to x and x to x includes information on the achievement of planned targets for the year and explanations provided for the under/overachievement of a significant number of targets. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 29 to 31 of this report.

Adjustment of material misstatements

31. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of basic service delivery. As management subsequently corrected only some of the misstatements, I identified material findings on the usefulness and reliability of the reported performance information. Those that were not corrected are reported above.

Introduction and scope

32. In accordance with the PAA and the general notice issued in terms thereof I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.
33. The material findings on compliance with specific matters in key legislation are as follows:

Annual financial statements

34. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of non-current assets, expenditure, and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

Liability management

35. Long-term debt was incurred without a resolution of the municipal council approving the debt agreement, in contravention of section 46(2)(a) of the MFMA.

Procurement and contract management

36. Some of the goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a).
37. Some of the invitations for competitive bidding were not advertised for a required minimum period of days, in contravention of SCM regulation 22(1) and 22(2). This non-compliance was identified in the procurement processes for the fleet management services.
38. Some of the competitive bids were adjudicated by a bid adjudication committee that was not composed in accordance with SCM regulation 29(2).

Budgets

39. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R50,99 million, as disclosed in note 44 to the annual financial statements, in contravention of section 62(1) (d) of the MFMA. The majority of unauthorised expenditure was caused by the overspending in individual departmental votes and unspent conditional grants not cash backed.

Expenditure management

40. Money owed by the municipality was not always paid within 30 days, as required by section 65(2) (e) of the MFMA.
41. An effective system of expenditure control, including procedures for the approval and authorisation of funds, was not in place, as required by section 65(2)(a) of the MFMA.
42. Effective steps were not taken to prevent irregular expenditure stated at R6,07 million which is disclosed in note 45 to the annual financial statements, as required by section 62(1)(d) of the MFMA. The full extent of the irregular expenditure could not be quantified as indicated in the basis for qualification paragraph. The majority of the disclosed irregular expenditure was caused by the municipality not following quotation process as well as deficiencies in the competitive bidding process followed.
43. Effective steps were not taken to prevent fruitless and wasteful expenditure amounting to R1,52 million, as disclosed in note 46 to the annual financial statements, in contravention of section 62(1) (d) of the MFMA. The majority of the disclosed fruitless and wasteful expenditure was caused by interest and penalty charges for late payments to suppliers.

Asset management

44. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

Revenue management

45. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.

Consequence management

46. Unauthorised expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a) of the MFMA.
47. Irregular and fruitless and wasteful expenditure incurred by the municipality were not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.

Other information

48. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report which includes the mayor's foreword, accounting officer's report and the audit committee report. The other information does not include the financial statements, the auditor's report and the selected development priority presented in the annual performance report that have been specifically reported in the auditor's report.
49. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
50. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected development priority presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
51. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information, if I conclude that there is a material misstatement therein; I am required to communicate the matter to those charged with governance and request that the other information be corrected. If the other information is not corrected, I may have to retract this auditor's report and re-issue an amended report as appropriate; however, if it is corrected this will not be necessary.

Internal control deficiencies

52. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon.
53. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for qualified opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

Leadership

54. Leadership did not exercise oversight responsibility regarding financial and performance reporting and compliance as well as related internal controls, this lack of the understanding the entity environment as well as key vacancies in key positions. Further to this the action plan was not properly monitored leading to various repeat findings.

Financial and performance management

55. The municipality did not keep full and proper records for financial and performance reports. Municipality did also not have understanding key legislation in which it must comply with, and identified non-compliances were not timely addressed.

56. Municipality did not prepare regular, accurate and complete financial and performance reports, this was mainly due to staff not fully understanding the financial and performance reporting frameworks.

Governance

57. The municipality did not implement appropriate risk management activities to ensure that regular risk assessments, including the consideration of information technology risks are conducted adequately and that a risk strategy to address the risks is sufficiently monitored.

Auditor-General

Pietermaritzburg

08 December 2017



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence

Annexure – auditor-general's responsibility for the audit

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for selected development priority and on the municipality's compliance with respect to the selected subject matters.

Financial statements

2. In addition to my responsibility for the audit of the financial statements as described in the auditor's report, I also:
 - identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control
 - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control
 - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the municipal manager, which constitutes the accounting officer
 - conclude on the appropriateness of the accounting officer's use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Mpofana Municipality's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of the auditor's report. However, future events or conditions may cause a municipality to cease continuing as a going concern
 - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation

Communication with those charged with governance

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and, where applicable, related safeguards.